

BEFORE THE STATE TAX APPEAL BOARD
OF THE STATE OF MONTANA

MARLIN & RUTH WILKE,)	DOCKET NO.: PT-1996-27
)	
Appellants,)	
)	
-vs-)	
)	
THE DEPARTMENT OF REVENUE)	FINDINGS OF FACT,
OF THE STATE OF MONTANA,)	CONCLUSIONS OF LAW,
)	ORDER and OPPORTUNITY
Respondent.)	<u>FOR JUDICIAL REVIEW</u>

The above-entitled appeal was heard on the 10th day of October, 1997 in Great Falls, Montana in accordance with the order of the State Tax Appeal Board of the State of Montana (the Board). The notice of the hearing was given as required by law.

The taxpayer, Marlin Wilke, presented testimony in support of the appeal. The Department of Revenue (DOR, represented by Marlyann Lawson and Richard Dempsey, appraisers, presented testimony in opposition to the appeal. Testimony was presented, exhibits were received, and a schedule for post-hearing submissions was established. Upon receipt of those submissions, the Board then took the appeal under advisement.

The Board, having fully considered the testimony, exhibits, and all things and matters presented to it by all

parties, finds and concludes as follows:

STATEMENT OF THE ISSUE

Is the change in classification from commercial to residential appropriate for the subject property?

FINDINGS OF FACT

1. Due, proper, and sufficient notice was given of this matter and of the time and place of the hearing. All parties were afforded the opportunity to present evidence, oral and documentary.

2. The record remained open for the receipt of three post hearing submissions from the DOR and the response from the taxpayer.

DOR submission requests:

1. A copy of the official policy adopted by the DOR to institute the property classification change of commercial back to residential.
2. Response to whether the 1993 State Tax Appeal Board Order was applied to the subject property for tax years 1993, 1994 and 1995.
3. Clarification of the assignment of the project to convert back to residential classification originally constructed residential properties which had been changed to commercial rental properties.

3. The taxpayers are the owners of the property which is the subject of this appeal and which is described as:

Improvements only upon Lot 9, Block 299,
Great Falls Original Townsite, Great
Falls, Cascade County, State of Montana.

4. The DOR appraised the subject improvements for
the 1996 tax year at a value of \$37,800.

5. The appeal form indicates that the taxpayer filed
an AB-26 Property Review Form on 6-8-96.

6. The taxpayers appealed to the Cascade County Tax
Appeal Board on November 11, 1996, stating:

Property was moved from Commercial
Classification to residential with no
change of use. Recent State Tax appeal
set building value at 27,700 (sic).
property (sic) across alley sold for
22,500 (sic) with new foundation.

7. In its July 30, 1997 decision, the county board
disapproved the appeal for the following reasons:

After hearing testimony and reviewing
exhibits the Board feels the original
intent of the bldg. was that of a single
family residence, therefore, Dept. of
Revenue is correct in appraising the
property as residential with a value of
\$37,800.00 for the bldg. and \$10,000 on
the land. This appeal is disapproved.

8. The taxpayers appealed the county board decision
to this Board on August 11, 1997, stating:

Property was moved from Commercial
Classification to residential with no
change of use on structure. Recent State
Tax appeal set building value at
\$27,700.00

9. The Order in Marlin & Ruth Wilke v. Department of Revenue, PT-1993-2450, states:

IT IS THEREFORE ORDERED by the State Tax Appeal Board of the State of Montana that the subject shall be entered on the tax roll of Cascade County by the Assessor of said County at the 1993 tax year value of \$10,000 for the land and the improvements value reflective of the removal of the ECF of 109%.

The values before this Board at that hearing as determined by the DOR were \$10,000 for the land and \$27,700 for the improvements. The value for the improvements after implementation of this Board's 1993 order is unknown to the Board since it was to be calculated by the DOR. Judicial review of this Board's decision was not sought by either party.

10. The DOR's post-hearing submission, received on October 17, 1997, states in summary:

RE: POST HEARING SUBMISSION

1. Enclosed please find a copy of the Policy statement dated 4-18-83 #83-2.
2. I did find out that the refund (sic) for the years 1993-1995 have been sent to the Cascade County Treasurer.
3. The Lead Commercial Appraiser and the Regional Manager made the decision to bring these properties back into compliance with the policy.

11. With the record still being open, Mr. Wilke and Mr. Dempsey were contacted by the Board telephonically on October 20, 1997. Both parties were questioned by the Board

and provided additional evidence and testimony.

12. The taxpayer's response to the post hearing submission was received on October 24, 1996. This response consisted of a written response along with copies of assessment notices from tax years 1990, 1991, 1993, 1993 revised, 1995, 1996 and 1997. Also attached were two AB-26 Property Review forms for tax years 1993 and 1996.

13. The valuation and classification history of the subject property is as follows:

- Taxpayer purchased property in 1987 for \$16,000.
- 1993 was the first year of that three year appraisal cycle.
- The taxpayer received an assessment notice dated June 4, 1993. The value indications were \$10,000 for the land and \$46,200 for the improvements.
- May 18, 1993 the taxpayer filed an AB-26 Property Review Form with the DOR and the classification was changed to commercial, thus, reducing the improvement market value to \$27,700.
- The taxpayer received a revised assessment notice dated November 12, 1993. The value indications were \$10,000 for the land and \$27,700 for the improvements.
- November 27, 1993 the taxpayer filed an appeal with the county tax appeal board. The DOR's improvement value was upheld by the county board.
- May 20, 1994 the taxpayer appealed the county board's decision to this Board.
- This Board ordered the DOR to reduce the value of the improvement by removing the application of a 109% economic condition factor.

- The taxpayer received an assessment notice dated May 8, 1996 . Upon contacting the DOR, the taxpayer was informed that the subject property's classification was changed from commercial back to residential. The DOR's market value for the improvement was \$37,800.
- May 8, 1996 the taxpayer filed an AB-26 Property Review Form with the DOR. The DOR determined the market value for the property was "fair & equitable".
- November 27, 1993 the taxpayer filed an appeal with the county tax appeal board. The DOR's improvement value was upheld by the county board.
- May 20, 1994 the taxpayer appealed the county board's decision to this Board.

14. The Cascade County Treasurer's office was contacted by this Board on October 17, 1997 to determine if the taxpayer had received a refund for tax years 1993, 1994 and 1995, pursuant to the Board's Order, PT-1993-2450. The Treasurer's office advised that the refund had been processed for the years 1993, 1994 and 1995 on October 16, 1997.

TAXPAYER'S CONTENTIONS

The taxpayer received an assessment notice in 1996 indicating a value change for the subject improvement. The improvement classification was changed from a commercial to a residential designation. Mr. Wilke stated that the property is a rental duplex and the previous owner operated it as a rental property. The use of the property has not changed; therefore, the value of the property should remain unchanged.

The subject property was originally constructed as a single family residence. The property has been converted to a two unit rental property, and this is illustrated by the physical features, separate metering, and the rental income.

DEPARTMENT OF REVENUE'S CONTENTIONS

Mr. Dempsey stated that he was assigned a project to identify residential properties which had been converted to commercial rental properties and classified as such. He was to return these to single family residential classification based on original construction and original use. Mr. Dempsey presented what he identified as the DOR policy on the "Valuation of Residence converted to Income Producing Property" (exhibit A). In summary, this exhibit states the following:

PURPOSE: To define the procedures to be followed when single family residences which have been converted to income producing properties.

PROCEDURE: A structure will be valued as a single family residence if:

1. It was originally constructed as a single family residence and has been partially converted in income producing (e.g. - addition of a basement apartment, homes converted to a Bed & Breakfast).
2. It is rented but used as, and originally constructed as, a single family residence.

These structures may be valued using the market, cost, or income approach. To be market modeled (market approach) these structures must be coded "D" in field 500 of CAMA.

DOR exhibit D is an attachment to exhibit A which states in summary:

November 23, 1994

TO: All Property Assessment Employees

FROM: Karin Cazier, Administrative Secretary
Property Assessment Division

SUBJECT: Draft Procedure - Valuation of Residences
Converted to Income Producing Property

On the reverse side of this letter is a draft procedure for the above referenced subject. Please review and send any comments to me by December 9.

The DOR's post-hearing submission with respect to the policy states, in summary:

EFFECTIVE DATE 4-18-83

SUBJECT: Valuation of Residences Uses as Rental property

A structure will be valued as a single family residence when:

1. It was originally constructed as a single family residence and has been partially converted into income producing property (e.g. - addition of basement apartment).
2. It is rented but used as and originally constructed as a single family residence.

Mr. Dempsey stated that the implementation of this policy affected approximately 125 properties. Subsequently, the classification of these 125 properties was changed from commercial to residential.

Mr. Dempsey was asked by the Board how this change in classification came about, who instructed him to implement the policy, and was he instructed to make the change for tax year 1996. Mr. Dempsey responded in the hearing and by post-

hearing submission that he was made aware of the policy and he was assigned this project by DOR supervisors. Mr. Dempsey stated in the post hearing submission:

The Lead Commercial Appraiser and the Regional Manager made the decision to bring these properties back into compliance with the policy.

Mr Dempsey also stated that he took it upon himself to make the change for tax year 1996.

DISCUSSION

With the record still open, the Board contacted Mr. Wilke and Mr. Dempsey telephonically on 10/21/97. Additional evidence and testimony was provided. When asked if the taxpayer received a revised assessment notice subject to 15-8-601, Mr. Dempsey responded "he did not receive a revised assessment notice". "He received an assessment notice for the year 1996 which had been corrected--changed back to residential".

The DOR has the authority to correct an assessment as provided in §15-8-601 MCA.

§15-8-601 MCA. Assessment revision - conference for review. (1) (a) Except as provided in subsection (1)(b), whenever the department discovers that any taxable property of any person has in any year escaped assessment, been erroneously assessed, or been omitted from taxation, the department may assess the property provided that the property is under on ownership or control of the same person who owned or controlled it at the time it escaped assessment, was erroneously assessed, or was omitted from taxation. All revised assessments must be made within 10 years after the end of the calendar year in which the original assessment was or should have been made.

(b) Within the time limits set by 15-23-116, whenever the department discovers property subject to assessment under Title 15, chapter 23, that has escaped assessment, been erroneously assessed, or been omitted from taxation, the department may issue a revised assessment to the person, firm, or corporation who owned the property at the time it escaped assessment, was erroneously assessed, or was omitted from taxation, regardless of the ownership of the property at the time of the department's revised assessment...

(3) (a) Notice of revised assessment pursuant to this section must be made by the department by postpaid letter addressed to the person interested within 10 days after the revised assessment has been made. If the property is locally assessed, the notice must include the opportunity for a conference, on the matter, at the request of the person interested, within 15 days after the notice is given...

In 1993 the DOR changed the value of the subject property subsequent to the filing of the AB-26 Property Review Form, and the DOR sent the taxpayer a clearly marked "revised" assessment notice.

The property record card indicates that the subject property was visited by the DOR on September 25, 1995 and Mr. Dempsey stated that he was the reviewing appraiser.

When the DOR changed the classification of the subject property for tax year 1996, the taxpayer should have received a revised assessment notice pursuant to §15-8-601 MCA. Ms. Lawson stated the taxpayer receives an assessment notice each year because there is personal property with the real estate; therefore, that's how the taxpayer was notified of the DOR's classification change. When the taxpayer responded to the DOR's classification change. When the taxpayer responded to the DOR's post-hearing submission, he submitted a copy of the

1996 assessment notice which is dated May 8, 1996. Nowhere on this notice is it marked revised.

It is the opinion of this Board that the DOR did not properly notify the taxpayer of the classification change as defined in §15-8-601 MCA. It is also the opinion of this Board that the DOR has selectively reappraised the subject property along with other commercial properties which were converted back to residential classification. Authority was not cited, i.e. case law, the Montana Code Annotated, or Administrative Rules, allowing the DOR to selectively reappraise property during an appraisal cycle. Mr. Dempsey's testimony that there may be 125 properties that were handled the same as the subject property widens the scope of this reappraisal activity.

Following the DOR's post-hearing submission, Mr. Dempsey admitted that exhibit A, the Draft Policy had never been finalized and adopted, thus, never implemented by the DOR. Exhibit A has, therefore, been made part of the record but is considered relevant only to the extent that the DOR may have contemplated some sort of change. Mr. Dempsey supplied the Board with the original policy which is dated 4/18/83 and which was in effect at the time the subject property was reclassified. That policy states in summary:

A structure will be valued as a single family residence when:

1. It was originally constructed as a single family

residence and has been partially converted into income producing property (e.g. - addition of basement apartment).

2. It is rented but used as and originally constructed as a single family residence.

What was never made clear by Mr. Dempsey is why the DOR chose to second-guess decisions made at the beginning of the 1993 appraisal cycle by its own appraisers. This property classification was changed by the DOR through the AB-26 process. That change was essentially upheld by the local tax appeal board and this Board. The DOR did not appeal either of those decisions to the District Court. (finding #13).

The Board agrees with the DOR and the taxpayer that this property was originally constructed as a single family dwelling. It cannot be ignored, however, that the subject property has undergone extensive reconditioning to convert it to a multi-unit or duplex property. There is separate metering for each unit, each unit has its own kitchen facilities, and each unit has access from the outside. The functional utility of the upper floor, when considering this as a single family dwelling, is significantly compromised. Interior access to the second floor is non-existent; access to each of the two units is from the exterior of the property.

In determining the market value for a property, an appraiser must consider the definition of market value. Market

value as defined in §15-8-111 MCA:

Assessment - market value standard - exceptions... (2)
(a) Market value is the value at which property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of the relevant facts...

It's expected that a potential buyer of this property would consider the physical characteristics. In addition, the subject property has been used as a rental property; therefore, this would lead a potential buyer to research the operating history, i.e. income and operating expenses.

Within the appraisal process, the highest and best use analysis is another factor to be considered in determining the market value. Is the use legally permissible, physically possible and financially feasible? The current use of a property cannot be ignored in the highest and best use analysis. To convert the property to a different use or to rehabilitate or remodel the existing use, the highest and best use of the property may be altered. The costs involved must be considered and can these cost be recouped in the sale of the property. The taxpayer testified that the subject property's foundation is in poor condition along with the exterior stucco siding. No cost estimates for needed repairs or conversion costs were presented.

The DOR's "Policy Statement" states in part:

1. It was originally constructed as a single family residence and has been partially converted into

income producing property (e.g. - addition of basement apartment).

It is the Board's opinion that the subject property has been more than partially converted, as contemplated in the first item on the post-hearing submission "Policy Statement". It is also this Board's opinion that the subject property can be identified as commercial by physical characteristics and past operating history.

Ms. Lawson stated that the market value determined by the DOR was derived by the sales comparison approach, but the "Montana Comparable Sales" sheet could not be reproduced because of the 1997 reappraisal. When asked if any of the sales selected to value the subject property were single family residences converted to duplexes, the DOR appraisers indicated they were unsure.

The Board is puzzled why the DOR ignored the January 17, 1996 Order in PT-1994-2450. It was determined that it was not until after this hearing that the value was adjusted and the taxpayer received refunds due for tax years 1993, 1994 and 1995.

15-2-310 (5) MCA The decision of the state tax appeal board is final and binding upon all interested parties unless reversed or modified by judicial review. Proceedings for judicial review of a decision of the state tax appeal board under this section are subject to the provisions of 15-2-303 and the Montana Administrative Procedure Act to the extent that it does not conflict with 15-2-303.

The taxpayer is, therefore, entitled the benefit of this Board's decision for tax years 1993, 1994 and 1995.

CONCLUSIONS OF LAW

1. The State Tax Appeal Board has jurisdiction over this matter. §15-2-301 MCA

2. §15-8-601 MCA. Assessment revision--conference for review.

3. §15-1-101 MCA. (1)(d) The term "commercial", when used to describe property, means property used or owned by a business, a trade, or a corporation and defined in 35-2-114 or used for the production of income, except property described in subsection (1)(d)(ii).

4. It is true, as a general rule, that the appraisal of the Department of Revenue is presumed to be correct and the taxpayer must overcome this presumption. The Department of Revenue, however, should bear a certain burden of providing documented evidence to support its assessed value. Western Airlines, Inc. v. Catherine J. Michunovich, et al, 149 Mont. 347.428 P.2d 3.(1967).

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ORDER

IT IS THEREFORE ORDERED by the State Tax Appeal Board of the State of Montana that the subject property shall be classified as commercial property and be entered on the tax rolls of Cascade County by the assessor of that county at the 1996 tax year value consistent with the previous State Tax Appeal Board Order, PT-1993-2450.

Dated this 4th day of November, 1997.

BY ORDER OF THE
STATE TAX APPEAL BOARD

PATRICK E. McKELVEY, Chairman

(S E A L)

GREGORY A. THORNQUIST, Member

LINDA L. VAUGHEY, Member

NOTICE: You are entitled to judicial review of this Order in accordance with Section 15-2-303(2), MCA. Judicial review may be obtained by filing a petition in district court within 60 days following the service of this Order.